Testimony on Maryland SB 511

Senate Budget & Taxation Committee

February 3, 2021

Thank you Chair Guzzone, Senate Budget & Taxation Committee Members, and Senator Pinsky.

On behalf of the Global Business Alliance (GBA), I urge the committee to consider the potential negative impacts of SB 511. This bill, as currently written, would make Maryland less competitive for foreign direct investment (FDI) and further hinder economic recovery efforts during such an unpredictable time.

GBA represents 200 American companies with a global heritage, including over 60 Maryland employers. You can find out more information about our members as well as ways they are helping combat COVID-19. International companies employ nearly 117,000 jobs in Maryland with 23 percent of these jobs in manufacturing. Over the past five years, employment from international companies has grown by 15 percent, which out-paced the state's overall private-sector growth of seven percent.[1] Nationally, on average, these firms pay American workers nearly $83,000 annually in wages and benefits.

Key Concerns & Potential Impacts

While we appreciate the strain that state government budgets have experienced due to the pandemic, we are concerned that one of the bill's provisions targeting foreign unitary members with any U.S. source income is extraordinarily sweeping. Of the more than 20 states that have implemented combined reporting, no state has employed a U.S. source income provision.

Under SB 511, as currently written, a taxpayer's combined return would have to include "income derived from or attributable to sources within the United States." Taxing this U.S.-source income could lead to the following consequences:

- **Hurt Efforts to Attract and Retain International Companies**: Taxing U.S.-source income would lead to extraterritorial double taxation, as this income is already taxed by the country in which it is received. This double taxation would make investments and expansions in Maryland more expensive for major employers.

[1] All statistics in this testimony are the latest available data from the U.S. Department of Commerce, Bureau of Economic Analysis (BEA) data released November 2020.

- **Damage Competitiveness**: Taxing U.S.-source income would differ from the "effectively connected income" (ECI) standard utilized by the Internal Revenue Code and many states to tax non-U.S. companies.[2] This would misalign Maryland's tax approach with other state and federal tax norms.

- **Increase Complexity Without Strong Water's Edge:** As written, SB 511 would distort traditional norms of the water's edge methodology by including foreign affiliates with income "derived from or attributable to sources within the United States" in the combined group. Every state with combined reporting has opted for a true water's edge methodology which does not simply include all US source income as income of unitary non-U.S. companies. This approach creates significant complexity and compliance burdens, where reporting misaligns with other state requirements and the federal corporate income tax.

- **Create Disputes with Treaty Partners**: Bilateral tax treaties ensure Maryland employers do not face double taxation on U.S.-source income. In the past, some foreign governments have enacted retaliatory action in response to states seeking to adopt a tax structure without a true water's edge system.

- **Override Addback Exceptions**: Maryland already addresses abusive related party transactions with expense deduction "addback" rules. These rules provide specific exceptions for legitimate business transactions including an exception for those located in treaty countries. The US source income provision effectively overrides the exceptions to the expense deduction addback rules.

Conclusion

Without a modest modification to either delete the U.S. source income provision or add an effectively connected income (ECI) standard, this legislation could put the state at a competitive disadvantage to its neighboring states. The Global Business Alliance can be a resource to answer any questions you may have or assist with modifications that will keep Maryland a competitive place to do business.

Thank you for the opportunity to weigh in on SB 511. Please let us know if we can can be of further assistance. Please contact Meredith Beeson, Director of State Affairs at mbeeson@globalbusiness.org or (202) 770-5141.

[2] To name a few states that use the ECI standard, see West Virginia § 11-24-13f(a)(4); District of Columbia §47-1810.07(a)(2)(D); and New York S.B. 6359, A.8559 (Chapter 59).